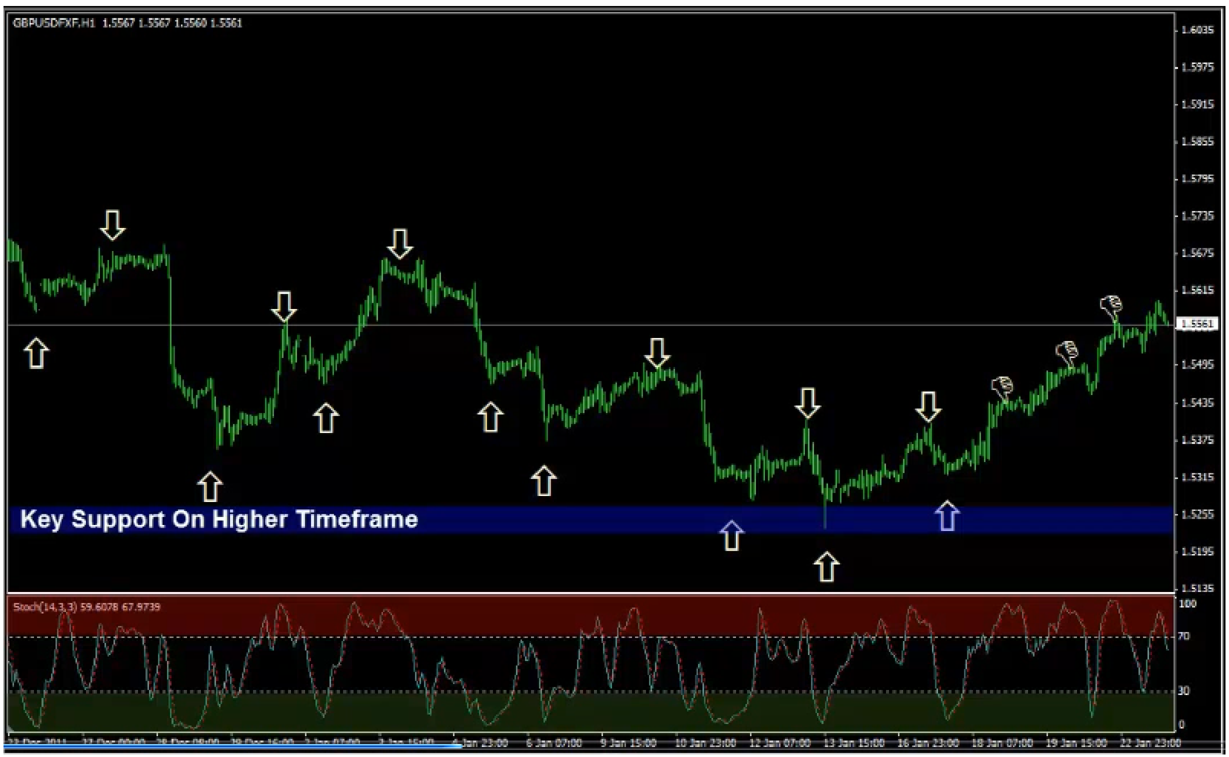
How Professionals Use Indicators

Wednesday, January 1, 2014   1:43 PM

- Using indicators will not be the answer in successful Forex trading.
- Indicators and charts do not move the markets or price itself, but price is what moves the indicators and charts.
- Indicators by themselves do not mean anything.

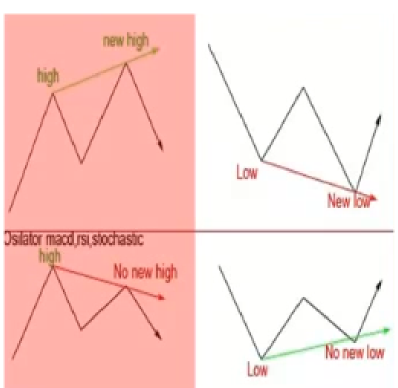
OVERBOUGHT & OVERSOLD

- The idea of overbought and oversold has probably resulted in the majority of trader's equity loss more than any single other "indicator" based concept.
- Focusing on oversold in markets that suggest that the market profile is bullish is the optimal use.
- Focusing on overbought in markets that suggest that the market profile is bearish is also optimal use.
- The image below shows how that once we hit key support on a higher time frame, it would only be logical to focus on the oversold readings in the stochastic and not the overbought ones. Oversold readings will generate more profitable trades for you:

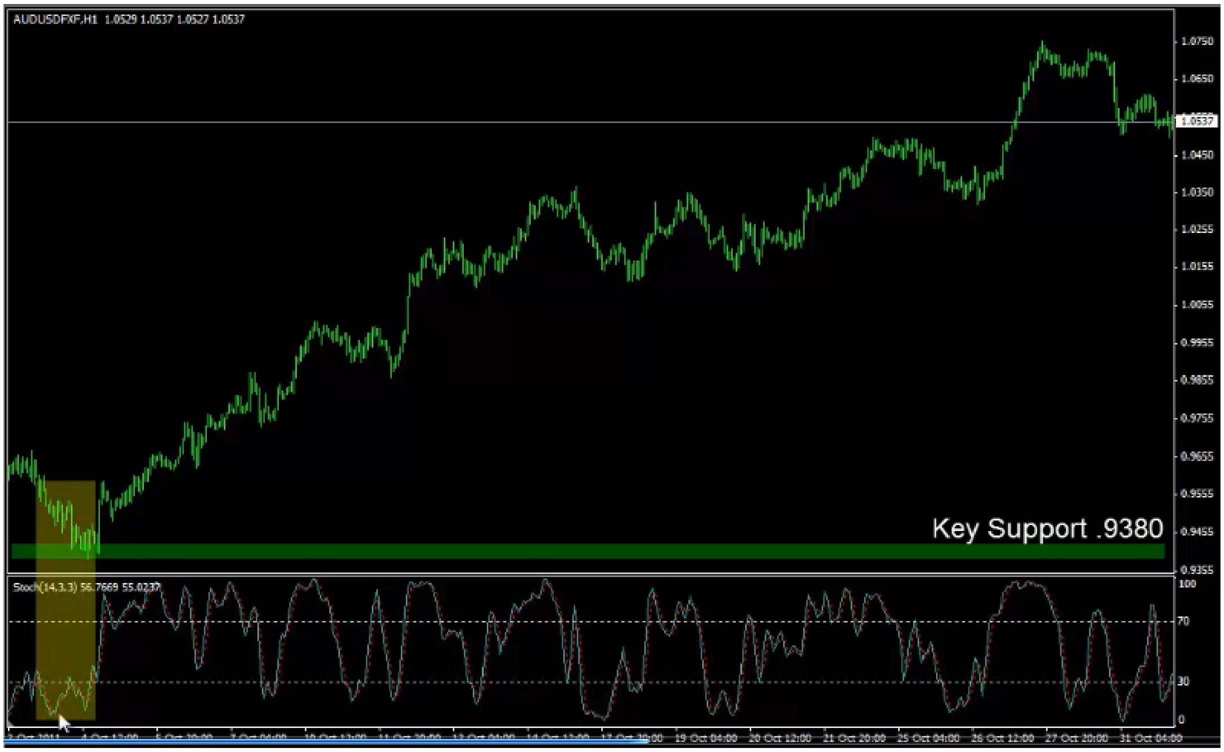


PRICE DIVERGENCES

- Divergence alone is useless without the higher time frame perspective.
- Highlighted in red below is an example of bearish divergence, the right side of the image is an example of bullish divergence:



- In bearish divergence, price makes a higher high and the indicator fails to make a higher high.
- In bullish divergence, price makes a lower low and the indicator fails to make a lower low.
- The image below shows an example of bullish divergence at key support which resulted in a nice upswing. Price made a lower low and the Stochastic oscillator failed to do so. This is called "type 1 bullish divergence":



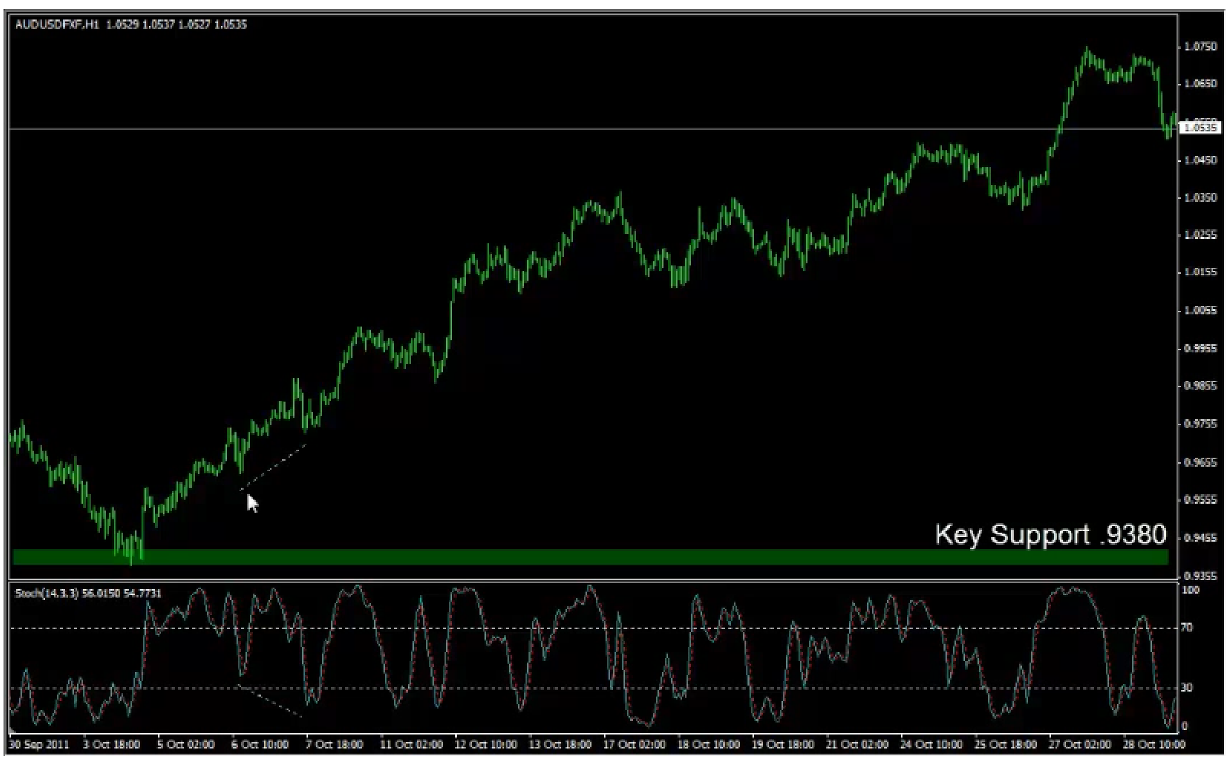
- Below is an example of a type 1 bearish divergence, in an uptrend all it does is give us consolidation into a retracement:



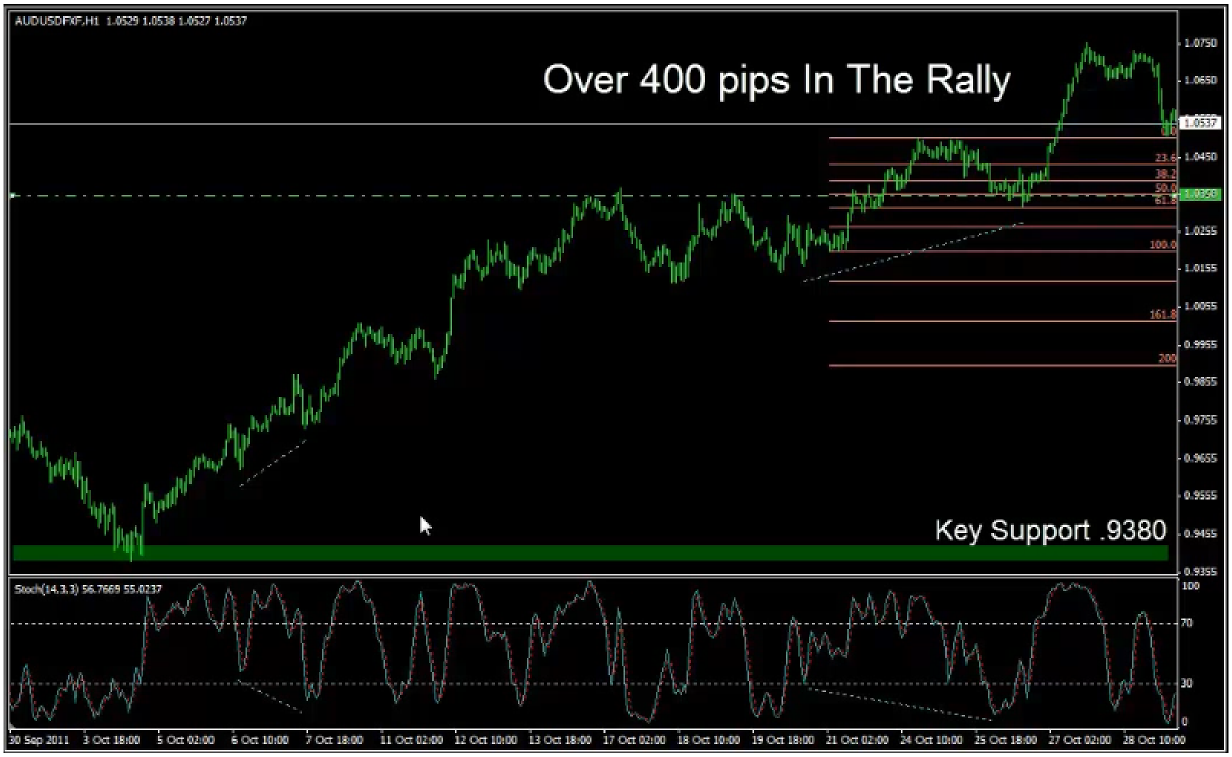
- Now we get one that is in sync with the higher time frame and it would have worked out much better:



- Using divergence with high time frame analysis and your indicators will become "magical."
- Below is an example of a trend following type 2 bullish divergence. In this case the indicator made a lower low while price failed to do so:



- A type 1 bullish divergence within a type 2 bullish trend following divergence is an extremely strong pattern. That is considered an ICT stinger entry signal. It works extremely well within a bullish market structure.
- It is also only powerful when you include support & resistance and optimal trade entry like in the image below:



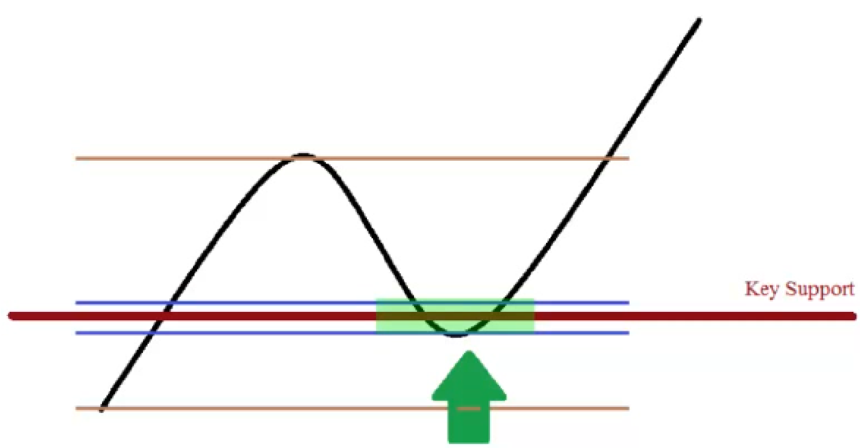
- Type 2 trend following divergence is also known as "hidden" divergence and Nick Van Nice discovered it.

TIME & PRICE THEORY

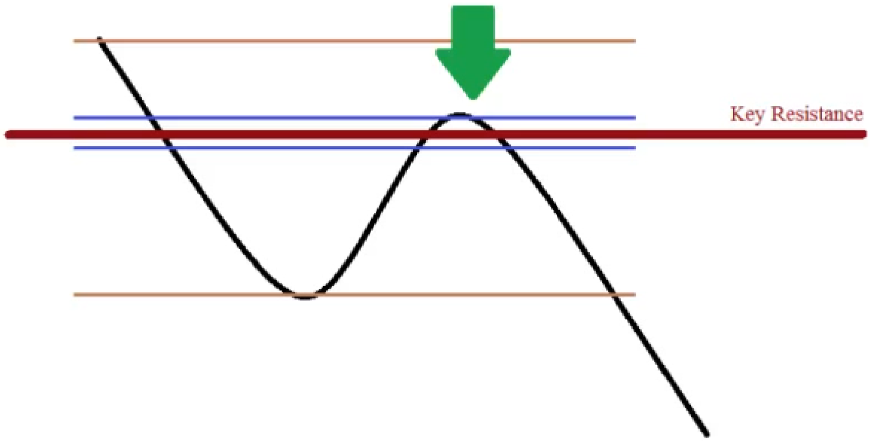
When and how do traders use indicators?

1. Determine key high time frame S/R levels (monthly, weekly, daily, 4 hour, MAYBE 1 hour).
2. Determine market structure and trend (4 hour and daily are your best friends here).
3. Determine market flow on HTF charts (daily, 4 hour, 1 hour).
4. Look for indicators to signal confirmation.
5. Filter out signals against higher time frame.
6. Look for convergence with other tools.

- Only use indicators on trade ideas that you had before you had the indicator on.
- The indicator is the last thing you look at.
- The green arrow below is where you expect bullish divergence to occur.



- The green arrow below is where you would anticipate bearish divergence to occur.



- Indicators are best used in conjunction with price action analysis and with optimal market profile applications.